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ORD 1163-64

10 June 1964

MEMORANDUM FOR: Director of Logistics
THROUGH: Deputy Director for Science and Technology
SUBJECT: Application of Cost Plus Incentive Fee (CPIF)
Contracts to Office of Research & Development

1. Based on discussions earlier this year between representatives of DD/S&T and Procurement Division, this Office has been operating under the assumption that as a result of the conclusions reached at these meetings, the majority of our contracts, because of their exploratory R&D nature, would be negotiated on a cost-plus-fixed-fee basis. This seems to be quite appropriate in view of the difficulty, in most cases, of defining a precise work statement for these efforts and of estimating accurately the costs associated with that work. In recent weeks, however, it appears that a preponderance of these contracts have been, or are being, negotiated on a CPIF cost basis.

2. This Office, in principle, agrees with the CPIF concept when applied to appropriately-selected types of efforts, but must view with alarm any policy which pursues the CPIF approach as an end in itself. We believe the philosophy espoused by us also to be Agency policy. On the surface, while it may appear by simple arithmetic that a CPIF contract is saving the Government dollars on that contract, there are costs above and beyond the simple costs covered in the contractual document that must be considered by the group responsible for the technical management of programs involving such contracts.

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3. In particular, we are apprehensive about loss of technical flexibility due to the application of stringent cost-sharing formulas of the CPIF type wherein the contractor's fee varies sharply with a deviation from the estimated or target cost. Under these circumstances we expect, during the coming year, to see a markedly diminishing cooperative attitude on the part of contractors holding such CPIF contracts. In the past, minor assignments or change orders relative to technical emphasis and change of direction could be easily accommodated; now we must anticipate the processing of change orders for even minor assignments involving technical emphasis or direction. This, in effect, will require that technical personnel, already stretched thin by a heavy load of high-priority projects, will have to devote excessive time to the purely administrative aspects associated with these contracts, thereby reducing technical talent for programs and projects in general.

4. As a result, it may well be necessary for this Office, through DD/S&T, to seek additional personnel ceiling from the Executive Director - Comptroller in order to accomplish the missions assigned to it, if over-emphasis of this apparent CPIF policy is continued.

5. Complete statistics on the number of CPIF contracts and the strengths of the cost-sharing formulas are not available to this Office at this time, but insofar as we can determine, out of the last forty (40) actions requested, it would appear that there have been fully processed four (4) contracts, of which two are CPIF with formulas varying from 80/20 (considered a strong formula) to 58/42, which is almost a candidate for fixed price incentive. During the past three weeks we have been notified of five (5) additional contracts which have been signed by the contractors, all of which are CPIF. Information from other contractors seems to indicate a strong attempt to place cost incentive contracts with them also.

6. After this Office has passed on its request for contracts to Procurement, we are not informed as to contract negotiating policy on an individual contract until it has been negotiated, at which point we find out what type of contract we have and whether the formula is

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strong or weak. Furthermore, because of the late start of the Office of Research and Development and the emphasis on major high-priority programs, such as audio countermeasures, it appears that the full extent of this problem will not be known until final contracts are in hand. In order to avoid the serious impending problems referred to above, it is suggested that more selective determination be made as to whether a particular R&D contract be CPIF at all, and if it is in a category that is suitable for CPIF; that some indication of the strength of the proposed cost-sharing be discussed with this Office for the purpose of evaluating the potential impact of the contract on the over-all problem and whether, in fact, there are factors involved which could lead to arithmetic savings on paper but result in an over-all increase in cost and lack of full performance.

[REDACTED]

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